

Hong Kong, China

Yield Movements

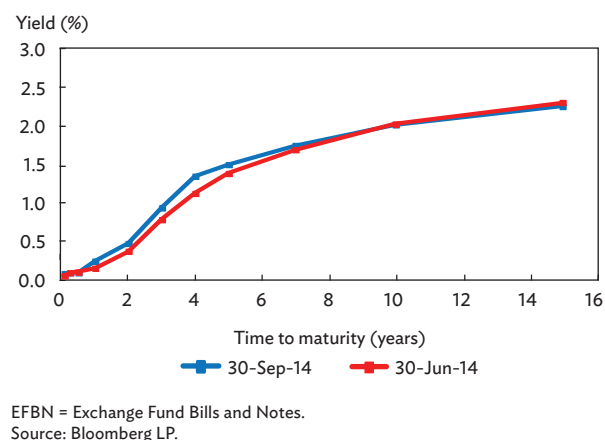
Between end-June and end-September, yields for Hong Kong, China's Exchange Fund Bills and Notes rose for most maturities, but fell slightly at the very long-end of the curve (**Figure 1**). Yields rose the most for the 3-year and 4-year tenors, rising 15 basis points (bps) and 22 bps, respectively. Hong Kong, China's 10-year and 15-year yields fell 1 bp and 5 bps, respectively. As a result, the 2-year versus 10-year spread narrowed to 153 bps at end-September from 164 bps at end-June.

Yield movements in Hong Kong, China tracked United States (US) interest rate movements in 3Q14, reflecting the Hong Kong dollar's peg to the US dollar. Yields on 3-year and 5-year bonds in the US rose 17 bps and 12 bps, respectively, while 10-year bond yields fell 4 bps.

Hong Kong, China's economy showed some improvements but risks remain. In August, retail sales recovered, rising 3.4% year-on-year (y-o-y) following a decline of 3.2% in July. However, the government noted that growth was partially boosted by the timing of the Mid-Autumn Festival. Looking forward, there are uncertainties related to changing tourist demand and external demand. Exports from Hong Kong, China rose 6.4% y-o-y in August after gaining 6.8% in July. However, the government is cautious, citing geopolitical risks and uncertainties regarding developed markets.

Inflation risk in Hong Kong, China remained moderate, although consumer price inflation rose to 6.6% y-o-y in September from 3.9% in August. According to the government, the increase was driven by a low-base effect last year due to public housing rental subsidies. As a result, the housing sub-sector of the Consumer Price Index rose 13.5% in September. Also, utilities prices rose 25.7% y-o-y due to the exhaustion of the government's one-time subsidy for some households. The government said that inflation should be stable in the near-term due to a lack of supply-side pressures.

Figure 1: Hong Kong, China's Benchmark Yield Curve—EFBNs



Size and Composition

The size of Hong Kong, China's local currency (LCY) bond market rose 0.5% quarter-on-quarter (q-o-q) and 0.3% y-o-y to reach HKD1,500 billion (US\$193 billion) at end-September (**Table 1**).

At end-September, the stock of government bonds comprising Exchange Fund Bills, Exchange Fund Notes, and Hong Kong Special Administrative Region (HKSAR) bonds rose 0.8% q-o-q to reach HKD856 billion. This was largely driven by an increase in outstanding HKSAR bonds as a result of a HKD10 billion issuance of 3-year HKSAR bonds under the Retail Bond Issuance Programme.

LCY corporate bonds outstanding remained unchanged on a q-o-q basis and fell 2.0% y-o-y to reach HKD645 billion at end-September, as companies preferred to raise funds via bank loans. In 3Q14, the five largest nonbank issuances came from Emperor International Holdings (HKD1.7 billion), Hong Kong Mortgage Corporation (HKD1.3 billion), Eastern Creation (HKD0.6 billion), CITIC Limited (HKD0.42 billion), and CLP Power Hong Kong Financing (HKD0.3 billion) (**Table 2**).

Table 1: Size and Composition of the LCY Bond Market in Hong Kong, China

	Outstanding Amount (billion)						Growth Rate (%)			
	3Q13		2Q14		3Q14		3Q13		3Q14	
	HKD	US\$	HKD	US\$	HKD	US\$	q-o-q	y-o-y	q-o-q	y-o-y
Total	1,496	193	1,494	193	1,500	193	0.5	9.7	0.5	0.3
Government	838	108	849	110	856	110	0.5	16.2	0.8	2.2
Exchange Fund Bills	682	88	684	88	684	88	0.1	16.0	(0.1)	0.2
Exchange Fund Notes	68	9	68	9	68	9	0.0	(0.9)	0.9	0.0
HKSAR Bonds	87	11	97	13	104	13	4.2	35.9	6.7	19.0
Corporate	658	85	645	83	645	83	0.5	2.4	0.0	(2.0)

() = negative, HKSAR = Hong Kong Special Administrative Region, LCY = local currency, q-o-q = quarter-on-quarter, y-o-y = year-on-year.

Notes:

1. Calculated using data from national sources. 3Q14 corporate bonds outstanding data carried over from 2Q14.

2. Bloomberg LP end-of-period LCY-US\$ rates are used.

3. Growth rates are calculated from LCY base and do not include currency effects.

Sources: Hong Kong Monetary Authority and Bloomberg LP.

Table 2: Notable LCY Corporate Bond Issuance in 3Q14

Corporate Issuers	Coupon Rate (%)	Issued Amount (HKD billion)
Emperor International Holdings		
3-year bond	5.00	1.65
Hong Kong Mortgage Corporation		
2-year bond	0.38	0.70
3-year bond	1.33	0.55
Eastern Creation		
3-year bond	2.35	0.60
Citic Limited		
10-year bond	4.35	0.42
CLP Power Hong Kong Financing		
15-year bond	3.78	0.30

LCY = local currency.

Source: Central Moneymarkets Unit (CMU) HKMA.

Corporate bonds outstanding from the top 30 nonbank issuers in Hong Kong, China amounted to HKD114.8 billion at end-September, representing about 17.8% of total outstanding corporate bonds. The top 30 list of issuers

was dominated by real estate firms (**Table 3**). HKMC remained the top issuer in Hong Kong, China with outstanding bonds of HKD14.6 billion. Next was CLP Power Hong Kong Financing with HKD10.6 billion of bonds outstanding, followed closely by Sun Hung Kai Properties with HKD9.9 billion. Among the top 30, five are state-owned companies and 11 are Hong Kong Exchange-listed firms. Only one state-owned company, the MTR Corporation, is listed on the exchange.

Policy, Institutional, and Regulatory Developments

Hong Kong, China Issues Debut *Sukuk*

On 10 September, Hong Kong, China issued its debut *sukuk* (Islamic bond). The *sukuk* was priced at a profit rate of 2.005%. The *sukuk* has an issue size of US\$1.0 billion and demand was strong with orders exceeding US\$4.7 billion. In terms of geography, buyers of the *sukuk* were diverse, with 36% going to the Middle East, 47% to Asia, 6% to Europe, and 11% to the US.

Table 3: Top 30 Nonbank Corporate Issuers in Hong Kong, China

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (HKD billion)	LCY Bonds (US\$ billion)			
1.	The Hong Kong Mortgage Corporate	14.57	1.88	Yes	No	Finance
2.	CLP Power Hong Kong Financing	10.65	1.37	No	No	Electric
3.	Sun Hung Kai Properties (Capital Market)	9.91	1.28	No	No	Real Estate
4.	Wharf Finance	7.03	0.91	No	No	Diversified
5.	The Link Finance (Cayman) 2009	6.14	0.79	No	No	Finance
6.	MTR Corporation (C.I.)	5.75	0.74	Yes	Yes	Transportation
7.	HKCG (Finance)	5.60	0.72	No	No	Gas
8.	Swire Pacific	5.53	0.71	No	Yes	Diversified
9.	Hongkong Electric Finance	5.51	0.71	No	No	Electric
10.	NWD (MTN)	5.05	0.65	No	Yes	Real Estate
11.	Cheung Kong Bond Finance	4.62	0.60	No	Yes	Real Estate
12.	Urban Renewal Authority	4.60	0.59	Yes	No	Real Estate
13.	Kowloon-Canton Railway	4.40	0.57	Yes	No	Transportation
14.	Wheelock Finance	4.04	0.52	No	No	Diversified
15.	Yue Xiu Enterprises (Holdings)	3.00	0.39	No	No	Diversified
16.	Airport Authority Hong Kong	2.80	0.36	Yes	No	Transportation
17.	Hysan (MTN)	2.43	0.31	No	No	Finance
18.	Cathay Pacific MTN Financing	1.70	0.22	No	Yes	Airlines
19.	Emperor International Holdings	1.65	0.21	No	Yes	Real Estate
20.	Nan Fung Treasury	1.31	0.17	No	No	Real Estate
21.	Henderson Land MTN	1.19	0.15	No	Yes	Finance
22.	AIA Group	1.16	0.15	No	Yes	Insurance
23.	Swire Properties MTN Financing	1.10	0.14	No	No	Real Estate
24.	Dragon Drays	1.00	0.13	No	No	Diversified
25.	K. Wah International	1.00	0.13	No	Yes	Real Estate
26.	Citic Limited	0.92	0.12	No	Yes	Diversified
27.	R-Reit International Finance	0.78	0.10	No	No	Real Estate
28.	Wing Tai Properties (Finance)	0.68	0.09	No	No	Real Estate
29.	HLP Finance	0.56	0.07	No	Yes	Real Estate
30.	The Hongkong Land Notes Company	0.20	0.03	No	No	Finance
Total Top 30 Nonbank LCY Corporate Issuers		114.84	14.82			
Total LCY Corporate Bonds		644.73	83.19			
Top 30 as % of Total LCY Corporate Bonds		17.8%	17.8%			

LCY = local currency.

Notes:

1. Data as of end-September 2014.

2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.

Source: *AsianBondsOnline* calculations based on Hong Kong Monetary Authority data.